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TAGS: [EFIN](#) [ECON](#) [IZ](#)
SUBJECT: IRAQ'S ECONOMY GROWING IN 2009, BUT JOBS STILL A
CONCERN

REF: A. BAGHDAD 350
[1](#)B. BAGHDAD 423
[1](#)C. PARIS 195

[1](#)1. (SBU) Summary: There is some good news in Iraq's macro-economic data, despite the global downturn and the collapse of oil prices. The economy should grow by at least 5 percent this year in real terms, provided the GoI can sustain spending growth. Core inflation should remain stable at about 12 percent. Despite the downward revisions in the draft 2009 budget, the GoI stands a good chance of completely executing its budget and surpassing last year's spending. However, continued low oil prices could force the GoI to draw down its accumulated fiscal assets quicker than expected, creating serious concerns for out years. Further, while real growth and public spending are likely to increase this year, the 2009 budget will not permit the GOI to make the investments necessary to improve long-term development, nor to meet the rapidly rising short-term expectations of a war-weary public. Recognizing the need to diversify its economy, Iraq, with USG and other international assistance, has intensified its focus on private sector development and is moving to address underlying constraints in its legal and regulatory framework. Unemployment is hard to measure, but creating more jobs remains the key short- and long-term goal for Iraq's economy. End summary.

Growth Slower But Still Strong

[1](#)2. (SBU) For Iraq's petroleum monoculture, a sharp fall in the price of oil counts as a serious shock. In a typical year, oil accounts for over 90 percent of GoI revenue and about two-thirds of Iraq's gross domestic product. As the bottom fell out of the oil market in the fourth quarter of 2008, the GoI significantly cut its 2009 budget projections. The word has gone out from the Ministry of Finance that public-sector wish lists have been trimmed, and hiring freezes are reportedly in place across the board.

[1](#)3. (SBU) But even with Iraqi oil selling for less than 40 percent of its 2008 peak, 2009 can be a good year for Iraq's economy. In its most recent staff report, the International Monetary Fund (IMF) projected real growth of 7.7 percent in 2009 for Iraq's economy. The latest forecast from the Economist Intelligence Unit is 6.1 percent. Both figures likely fail to take full account of slackening global demand for oil. But as long as the GoI can sustain spending growth, Iraq's economy should expand by at least 5 percent this year. That would be well below the 2008 growth of between 7 and 9 percent.

Core Inflation Stable at 12 Percent

[1](#)4. (SBU) Iraq's core price index, which excludes volatile energy prices, grew by 11.8 percent in 2008, a shade lower than the 2007 rate of 12.3 percent. Headline inflation for the 12 months through November was 6.8 percent. With food

accounting for nearly two-thirds of Iraq's current consumer price index, inflationary pressure should ease with the global decline in commodity prices.

¶15. (SBU) Over the past two years the Central Bank of Iraq (CBI) has allowed the dinar to appreciate against the U.S. dollar to check money-supply growth and stabilize core inflation at a level Iraqis have not seen in decades. In 2008 the dinar appreciated 3.6 percent against the dollar, a little more than half the rate of appreciation seen in 2007. With the GoI soon to be unconstrained by IMF conditionality, the CBI may find itself exposed to political pressure to slow the appreciation of the dinar even further. But this would not necessarily re-ignite the rampant inflation Iraq experienced in 2006 before the dinar's appreciation. Qexperienced in 2006 before the dinar's appreciation.

Revenue is Down, But Spending Can Grow

¶16. (SBU) The GoI's recent downward revisions in the 2009 budget (Ref A) need not result in a decline in spending. Iraq has not yet fully executed a post-invasion budget, so the immediate effect of a cut in spending plans is to bring projected outlays closer to the level the GoI is able to spend. Implementation of the 2008 budget supports this idea. As of November 2008, USD 41 billion of the total USD 50 billion budget had been spent. By comparison, in November 2007 the GoI had spent only USD 23 billion of that year's budget. Thus, for 2009 the GoI stands a good chance of completely executing its budget of USD 60 billion or so. In that event, spending would increase nearly 20 percent over 2008's level, or about 8 percent in real terms.

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¶17. (SBU) Depending on the direction oil prices take in the coming months, the GoI could conceivably draw down quicker than expected its accumulated fiscal assets in the Development Fund for Iraq and on deposit at the CBI or in state-owned banks. The draft 2009 budget foresees expenditures of USD 63 billion and a deficit of USD 20 billion, assuming an average oil price of USD 50 per barrel and daily export sales of 2.0 million barrels per day. If, as is likely, these budget assumptions prove to be optimistic, the GoI could curtail spending, as it presaged in the December review of its IMF Stand-by Arrangement, and possibly act to increase its domestic borrowing. Indeed, the Finance Minister recently announced that the Ministry would activate the treasury-bill market to borrow up to USD 5 billion (Ref B). However, a senior MOF advisor advised us that such an offering would not be in the immediate future.

Unemployment Hard to Gauge

¶18. (SBU) Iraq's continued strong economic performance is largely a consequence of improved security conditions. Further improvement is needed, but already Iraqis are able to turn their attention to quotidian concerns beyond security. Like jobs. Progress on this front is still hard to gauge, and is made more challenging by already-bloated public-sector payrolls. The GOI's official estimate of the unemployment for 2006 was 17.5 percent, and the 2008 figure was reportedly 18.2 percent. The 2007 Iraq Household Socio-Economic Survey (IHSES), supported by the GoI and the World Bank, indicated an overall unemployment rate of 11.7 percent. Other sources have suggested jobless rates three or even four times this level. According to GoI figures, 48 percent of the Iraqi workforce is either unemployed or underemployed.

Public Focus on Private Sector Development

¶19. (SBU) The need to develop Iraq's private sector has been a theme the GoI has often mentioned, but rarely addressed in a

concerted or dedicated manner. Security improvements mean that "lack of security" can no longer be the scapegoat for all of Iraq's economic development woes. The World Bank and the United Nations are focused on assisting Iraq with its private sector development, and Iraq insists it is making an earnest effort to streamline the bureaucratic obstacles (Ref C). The USG is supporting these efforts through on-going programs and implementation of the Strategic Framework Agreement.

Comment

¶10. (SBU) Whichever unemployment number one chooses to believe, there is no dispute over the need to expand employment opportunities in Iraq. As one of our Iraqi colleagues put it recently, "Everyone wants more electricity, but what Iraqis really need is jobs." The dilemma is that, while five percent growth is respectable in the face of a global recession, it is not likely to be sufficient to meet the demand of Iraq's war weary population. While Iraq's accumulated fiscal surpluses provide the means to keep public sector spending at the level required to generate positive growth (critical in an election year), the low oil prices will severely constrain the GOI's ability to invest in capital projects critical to long-term economic development. To its credit, the GOI is not resting on the fact that 2009 will be a relatively good year for the economy: officials from the prime minister down are emphasizing the need to take immediate steps to accelerate development of the non-oil economy (in addition to improving performance of the oil sector) in order to avoid more serious economic hardship down the road.

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